

### **SECTION 3: THE GEOSTRATEGIC IMPACT OF CHINA'S ENERGY POLICIES AND ACTIVITIES**

“The Commission shall investigate and report on—

“ENERGY—The effect of the large and growing economy of the People's Republic of China on world energy supplies and the role the United States can play (including joint research and development efforts and technological assistance), in influencing the energy policy of the People's Republic of China.”

#### **China's Search for Energy Security and the Impact of Pursuing Equity Oil**

China's concern over access to resources including oil has become an important influence on its strategic behavior.<sup>156</sup> Mr. David Helvey, Country Director for China, Taiwan, and Mongolia for the U.S. Department of Defense, testified to the Commission that “China's response to its energy needs has led Beijing to finance energy projects that have uncertain prospects for a positive return on investment, to ignore political risk that is prohibitive to private commerce, and to establish closer relations with problem states that are rich in energy but that defy international norms.”<sup>157</sup> These steps entail significant risks, confirming the great importance China's leadership attaches to pursuing a sufficient energy supply.

China's energy-related actions reflect its distrust of international oil markets—which it sees as primarily dominated by the United States—and call attention to the motivations behind China's national “going-out” strategy described in Chapter 3, Section 1. In order to ensure an adequate petroleum supply for its domestic consumption needs, China has chosen to establish long-term supply contracts to purchase oil produced in other nations, rather than relying on the market-based acquisition mechanisms of the international oil market; and to encourage its companies to pursue ownership of oil production in overseas fields. This approach, based on what essentially is a zero-sum perspective of the global oil market, challenges the current multilateral perspective on energy cooperation.<sup>158</sup>

This policy has political and security consequences for China. The “going-out” strategy supports the expansion of China's oil companies into overseas oil production and the acquisition of equity oil contracts to develop and produce new resources (see Chapter 3, Section 1). Congruent with this policy is China's overall foreign policy approach that seeks to expand China's influence around the world and promote a perception that China is willing to offer aid

and development assistance to developing nations while not interfering in their internal affairs. Thus, in the past, China's search for equity oil often has been supported by the development of official political relationships.

Witnesses testified to the Commission that China's national oil companies—while majority state-owned—may have begun to act independent from the government in their pursuit of the “going-out” strategy, and make investment decisions based on projected commercial returns rather than national policy (see Chapter 3, Section 1). Messrs. Daniel Rosen and Trevor Houser write in their paper “China Energy: A Guide for the Perplexed,” “[China National Petroleum Corporation] (CNPC), [China Petroleum and Chemical Corporation] (Sinopec), and [China National Offshore Oil Corporation] (CNOOC) have used political clout to get supportive high-level state visits, access to subsidized capital, or development assistance money designated for infrastructure projects. This sometimes contradicts Beijing's desire to sink additional investment into mature, less profitable fields at home in order to prop up declining domestic production.”<sup>159</sup> Mr. Mikkal Herberg, Research Director of the Asian Energy Security Program at the National Bureau of Asian Research, testified that the energy firms' actions, contradicting government preferences, may be linked to the companies' competitiveness. As the companies become more competitive internationally, they seek to be more independent from the government's influence. Moreover, their interests may diverge from the state's interests.<sup>160</sup>

When the practices or actions of China's oil companies operating in other countries engender local discontent or international concern, Beijing must seek to repair relationships not only with the countries in which the problems have occurred, but also with international organizations and other nations that promote responsible activity by companies investing in developing countries.

Sometimes local antipathy to Chinese investments and activities endangers those investments and Chinese personnel who are implementing them. For example, in September 2006 Sinopec was ordered to halt all exploration operations in Gabon after it was discovered that the company was operating in a national park without having received approval from Gabon's Environment Ministry for its environmental impact study. “Sinopec was accused of dynamiting and polluting Loango National Park, tearing up the forest to create roads, and generally destroying the habitat . . .”<sup>161</sup>

In January 2007 Nigerian gunmen kidnapped nine Chinese employees of CNPC working in the southern state of Bayelsa and demanded ransom.<sup>162</sup> In April 2007 rebels attacked a Chinese-run oil field in Ethiopia, killing nine Chinese workers and kidnapping seven.<sup>163</sup> Although the Chinese workers were not directly targeted by the rebels, the Ogaden National Liberation Front released a message stating, “We will not allow the mineral resources of our people to be exploited by this regime or any firm [with which] it enters into an illegal contract.” In 2007 China conducted several exercises aimed at simulating hostage situations. Although these exercises generally were conducted within the context of counterterrorism and preparation for the 2008 Olympic Games, it is important to note that these skills could be applied by Chinese

special forces and People's Armed Police in any hostage situation that Chinese workers abroad might face.<sup>164</sup>

In particular, China's relationships with Iran, Burma, and Sudan have resulted in criticism from Western countries that prohibit their oil companies from operating in these countries for political and human rights reasons. China has resisted taking steps to resolve the political and human rights conflicts in Iran and Burma. It has supported some U.N. resolutions addressing Iran's nuclear program, but has not reduced its investments or activities pertaining to Iran's petroleum supplies. It has not supported U.N. resolutions addressing human rights problems in Burma or taken any other discernible action to seek a responsible solution there.

In Sudan, China recently has taken minimal steps to encourage the Khartoum government to accept the U.N.-African Union peacekeeping force and to discuss ways to address the genocide in Darfur. China has voted in favor of U.N. Security Council Resolution 1769, which established a U.N.-African Union hybrid peacekeeping force in Darfur (UNAMID) consisting of 19,555 military personnel.<sup>165</sup> China also has made statements that support peace in Sudan. The press reported that China's President Hu Jintao discussed the Darfur crisis with Sudanese President Omar al-Bashir during President Hu's visit to Sudan in January 2007.<sup>166</sup> And in May 2007 China appointed a special envoy to Sudan to convey its desires for the conflict there to be resolved responsibly, and publicly encouraged the government in Khartoum to accept U.N. and African Union peacekeepers. In October 2007 the government announced that the People's Liberation Army (PLA) was preparing to send a combat engineer battalion of 315 soldiers to provide engineering support to the U.N. peacekeeping mission in Darfur.<sup>167</sup>

China, however, has not been willing to risk its investment in Sudan in order to increase pressure on the Sudanese government to halt the genocide. It even has increased its aid for infrastructure projects in Sudan. For example, during the same visit in January 2007, President Hu offered an interest-free loan to Khartoum to build a new presidential palace. He cancelled \$80 million of debt, and announced a plan to invest in the construction of a new railroad.<sup>168</sup> China also has invested an estimated \$2 billion in the construction of the Merowe Dam, which is expected to supply all of Sudan's energy needs.<sup>169</sup> Further, China has continued to sell arms to the Khartoum government.

China's "hands off" approach to these nations rests ostensibly on its objections to interference in the internal affairs of one nation by another. It is likely that China's actions also are motivated by a desire to protect its investments and access to energy in those nations, as well as build relationships there. Whatever its explanation or motivation, China at best has failed to help resolve these matters in a manner acceptable to the world community, and at worst has acted as an "enabler" to the abusive regimes in these nations while stymieing or at least complicating international efforts to resolve the political conflicts, humanitarian crises, and rights violations occurring there.

Mr. Herberg testified that there are signs that China is changing its approach, although it is premature to conclude that has occurred. The influence of public awareness campaigns that encour-

age the Chinese government to divest itself of its investments in Sudan, and have linked this issue to the 2008 Olympics in Beijing, has created a policy conundrum for China.<sup>170</sup> China's passive approach to addressing its activities in Sudan and their implications could have an economic impact. In May 2007 Fidelity Investments reduced its stake by 91 percent in PetroChina Co., CNPC's listed subsidiary on the New York Stock Exchange. (CNPC is the Chinese oil company with investments in Sudan.)<sup>171</sup> China's passive approach to this issue also is affecting the way in which China is perceived around the globe.

China must balance its desire to maintain its investments in Sudan's oil production, one of its largest overseas sources of equity oil, with its desire to be perceived as a responsible international power that at the very least condemns genocide. Although witnesses testified to the Commission that China most likely will not divest its holdings in Sudan, they expressed the belief it will become more active in urging Khartoum to pursue a more reasonable course and to obtain a resolution to the violence in Darfur.<sup>172</sup> As noted above, China has taken a few, limited steps that suggest this view is correct.

### **Global Security Implications**

Three primary concerns dominate discussions about the strategic consequences of China's energy consumption, and all three relate to China's access to and consumption of oil. First, China's strategy of acquiring equity oil overseas is an attempt to lock up supplies that, in a time of crisis, could significantly affect the global oil market and, subsequently, the United States' ability to acquire oil. Second, China increasingly is willing to expend political capital through its foreign relations and commercial relationships to protect its access to energy supplies. And third, China has expressed and demonstrated willingness to designate military resources to ensure that the transit to China of oil it has produced or obtained in other nations is protected.

### ***The Role of Energy Security in China's Naval Modernization***

China has openly expressed the intention to protect its investments abroad, especially its energy supplies. In December 2006, when meeting with representatives of the PLA Navy at the Chinese Communist Party's national congress, President Hu called for a navy capable of defending China's maritime interests and rights.<sup>173</sup> In July 2007, Commander of the PLA Navy Wu Shengli and then-Political Commissar of the Navy Hu Yanlin, wrote:

*Our nation is an oceanic nation that owns more than 18,000 kilometer[s] of oceanic coastline, more than 6,500 islands that are larger than 500 square meters, more than three million square kilometers of oceanic area with sovereignty and jurisdiction, and international exclusive exploitation right for 75,000 square kilometers at the bottom of the Pacific. In the oceanic area of our nation, there exist huge strategic interests along with various contradictions and threats. ... In order to ... maintain the safety of oceanic transportation and the strategic passageway for energy*

*and resources, ensure the jurisdiction of our nation to neighboring areas, continental shelf, and exclusive economic zones, and effectively safeguard our national maritime rights, we must build a powerful navy.*<sup>174</sup>

PLA military officers at the Academy of Military Sciences reaffirmed this perspective during discussions with the Commission's delegation to Beijing in April 2007.

Because the majority of China's oil imports transits through the Malacca Strait, Beijing views protection of the sea lines of communication (SLOCs) through this area as a priority for its energy security. Dr. James Holmes, Associate Professor at the Naval War College, testified to the Commission:

*From the perspective of international strategy, the Strait of Malacca is without question a crucial sea route. . . . It is no exaggeration to say that whoever controls the Strait of Malacca will also have a stranglehold on the energy route of China. Excessive reliance on this strait has brought an important potential threat to China's energy security.*<sup>175</sup>

Currently, the United States is the primary guarantor of the sea lines in the Strait of Malacca. In this respect, Dr. Holmes noted that "China is increasingly reluctant to entrust the security of shipping and thus its economic development to what it sees as the uncertain goodwill of the United States."<sup>176</sup>

China does not have the naval capability to assume responsibility for protecting its SLOCs through the Malacca Strait or, were it to see a need to do so, to challenge the U.S. naval presence in that area.<sup>177</sup> This relative weakness is the motivation for a range of steps China is taking to increase its military and nonmilitary options and to decrease its dependence on the Strait.

Dr. Holmes stated in his testimony that in addition to preparing for a possible conflict over Taiwan, resource security is a primary motivation for China's naval modernization. He cited Chinese scholars Liu Xinhua and Qi Yi, who wrote, "Ocean power has permanent meaning to the trade of coastal countries, and the backup of a country's ocean power is its navy. Therefore, the long term approach toward ensuring [open] sea lanes and [access to] potential ocean resources is to [develop] a modern ocean-going navy."<sup>178</sup> As discussed in Chapter 2, Section 1 on China's military modernization, over the long term it appears China may be moving beyond a concentration on developing littoral naval forces and may be beginning to build a blue-water navy that can engage in long-range missions and power projection.

DoD's 2007 *Annual Report to Congress on the Military Power of the People's Republic of China* reports that China's concern about this strategic weakness has prompted Beijing to pursue capabilities that "would help it ensure the safe passage of resources through international waterways."<sup>179</sup> Mr. Helvey noted several related military developments in his testimony, including:

1. *New missile units outfitted with conventional theater-range missiles at various locations in China could be used for anti-access/area denial in a variety of regional contingencies.*

2. *Airborne early warning and control and aerial-refueling programs could permit extended-range offensive air operations into the South China Sea.*
3. *Advanced destroyers and submarines equipped for anti-air, anti-surface, and undersea warfare could enable Beijing to protect and advance its maritime interests.*
4. *New equipment, better unit-level tactics, and greater coordination of joint operations are improving China's emergent expeditionary forces—at present, three airborne divisions, two amphibious infantry divisions, two marine brigades, about seven special operations groups, and one regimental-sized reconnaissance element in the Second Artillery.*
5. *Investment in command, control, communications, computers, surveillance, intelligence, and reconnaissance (C4ISR) capabilities, including space-based and over-the-horizon sensors, could improve identification, tracking, and targeting of foreign military activities deep into the western Pacific Ocean.*
6. *Extended long-range patrolling into the Indian Ocean is providing increased opportunities for PLA Navy crews to become familiar with the traditional sea lanes upon which their oil is shipped. China has conducted two multi-ship forays into the Indian Ocean this year, including one to participate in a multilateral naval exercise hosted by Pakistan, and the other to call on St. Petersburg, Russia.<sup>180</sup>*

Dr. Toshi Yoshihara, Associate Professor of the Naval War College, stated in his testimony that a benchmark for measuring Chinese change or progress in the development of these capabilities is to gauge the ability of China to conduct long-range maritime reconnaissance or replenishment operations.<sup>181</sup>

### ***How China Applies Soft Power to Aid Its Energy Security Efforts***

In the meantime, as these capabilities develop, China faces an “ambition-credibility gap,” as described by Mr. Helvey. To lessen the gap while undergoing military modernization, China is building a reservoir of soft power within Asia. Dr. Yoshihara referred in his testimony to Dr. Joseph Nye's definition of soft power, which is having “an appealing culture or political institutions [that engender] goodwill elsewhere in the world, helping a state's political leaders initiate collaborative actions involving other states.”<sup>182</sup> The use of soft power, including aid and investments, allows China to expand its presence and influence throughout Asia through cultural and political collaborations that seek to influence other countries' perceptions of China and dispel fears about China's military expansion.

For example, China has been negotiating basing rights along the coastline of South and Southeastern Asia, which has been termed its “string of pearls” strategy. According to Dr. Holmes, this strategy is allowing China to “[lay] the foundations of a strategic maritime infrastructure that would enhance both its economic prospects and its military access to the Indian Ocean.”<sup>183</sup> This strategy has produced concern among China's neighbors about its intentions. During the Commission delegation's visit to India in August 2007,

Commissioners were told that Indian policymakers view the “string of pearls” strategy as an attempt to expand Chinese economic, military, and political influence, while at the same time limit India’s role in the region. (See Chapter 4, Section 2 for elaboration.)

One pearl in the string in which China has invested is construction of the Port of Gwadar in Pakistan. This port is located strategically near the Strait of Hormuz, through which oil shipments leaving the Persian Gulf must transit. In the event the United States blocked China-bound ships from passing through the Malacca Strait, oil from the Persian Gulf or Africa could be offloaded from ships and transported overland from Gwadar to China. Dr. Holmes concluded, “Beijing might find the high price of such an alternative worth paying for assured energy supplies in the face of a U.S.-imposed embargo.”<sup>184</sup> Also, this port could serve as a future launching base for a Chinese presence in the Persian Gulf.<sup>185</sup> Although Dr. Holmes noted in his testimony that the Port of Gwadar is no “trump card” for China—given its geographical vulnerabilities and the capabilities of the U.S. Navy—he said that implementation of the “string of pearls” strategy will help China project power and influence well beyond the East and South China Seas and the Taiwan Strait.

Acquisition of new naval capabilities also may assist China in asserting territorial claims that have energy implications. China claims sovereignty over territory in the East and South China Seas involving areas contested by Japan, Taiwan, Brunei, Indonesia, Malaysia, Philippines, and Vietnam.<sup>186</sup> While these territories are not rich in resources above the surface, experts believe the areas contain significant amounts of oil beneath the ocean floor. This has been a motivating factor in China’s assertion of sovereignty over the disputed areas—which, according to Mr. Helvey, has contributed to regional tensions.<sup>187</sup> Tighter energy supplies and higher oil prices could motivate China to act more aggressively toward these claims. This could prompt other nations in the region to build up their own naval forces. The Malabar naval exercise in September 2007 that included the navies of the United States, India, Japan, Australia, and Singapore is an example of expanded military cooperation in the region. Previously, the exercise included only the United States and India.<sup>188</sup> Continued naval buildup may have the potential to increase regional tensions further. Mr. Helvey noted, however, that all parties involved in territorial disputes in the region currently appear to remain focused on resolving them diplomatically.<sup>189</sup>

China is able to emphasize a diplomatic approach toward this situation primarily because it has invested heavily in expanding its soft power influence in Asia. Dr. Yoshihara explained China’s motivations for such behavior:

*First, Beijing evidently hopes to allay suspicions in Asian countries wary of its great-power ambitions, forestalling U.S. or Asian opposition to its bid for sea power. Second, by assuaging regional anxieties about China’s rise, Beijing is seeking to foster perceptions that the nation’s return to the nautical area ... is not to be feared but rather embraced.<sup>190</sup>*

Moreover, Dr. Yoshihara argued that, in conducting this soft power campaign, China is attempting to persuade other Asian nations that its mastery of the seas is preferable to mastery by the United States, the self-appointed guarantor of the Asian sea lanes and [in China's opinion] the heir to the imperialist legacy. Thus, China promotes its naval ambitions by framing its actions in terms of "commerce and discovery" in contrast to the ambitions of the United States, which it implies emanate from Western powers' history of "imperial conquest and exploitation."<sup>191</sup> It does this in a variety of ways that seek to increase China's cultural appeal, create favorable perceptions of China's economic development model, and strengthen kinship ties to overseas Chinese in the region.<sup>192</sup>

Nonetheless, many Asian countries remain unconvinced that China's motivations and aspirations in the region are benevolent—or even benign. This opinion was reiterated in meetings the Commission delegation had in New Delhi with Indian security analysts and academics.

### ***China's Efforts to Diversify Its Acquisition of Energy Supplies***

Another component of China's energy acquisition and security strategy is establishment of land-based routes for transporting energy supplies from their sources to China. These routes will enable China both to diversify its energy supply sources throughout Central Asia and also to import energy via a route that does not pass through the Malacca Strait. Although these routes could not supply China with all its import needs, they could contribute to China's energy security in the event that the Malacca Strait was blocked.

"China has worked assiduously over the past decade to establish closer energy and diplomatic ties with Russia and the key Central Asian energy-rich states."<sup>193</sup> China has formally entered a Strategic Energy Alliance with Kazakhstan. China's investment in Kazakhstan currently provides it with 200,000 barrels of oil per day and the plan is to increase delivery up to 400,000 barrels per day in the next few years.<sup>194</sup> China signed an agreement in July 2007 with Turkmenistan for long-term supply of natural gas through a new pipeline that will connect the two nations. The terms of that agreement are unavailable publicly, and the volume of natural gas delivery for which it provides is not yet known.<sup>195</sup>

In addition, China has been attempting to improve its relationship with Russia, from which it has been receiving approximately 250,000 barrels per day of crude oil by rail, and with which it has been pursuing construction of pipelines to China—although this effort has not progressed at the pace China had hoped. Mr. Herberg noted in his testimony that the reason for this lag is that the bilateral relationship has been "fraught with cross-currents of competition, suspicion, and Russian energy policy paralysis. ..." <sup>196</sup> Regardless, he concluded that over the long term it is likely that the volume of oil and gas exports from Russia to China will increase.<sup>197</sup>

In Central Asia, China's diplomacy, including its establishment of and involvement in the Shanghai Cooperation Organization (SCO), is key to implementation of its energy policy. Given the cost and difficulty of constructing an oil pipeline, an oil-producing na-



tion must have a secure contract to make such construction financially justifiable. Establishing strong bilateral and multilateral relations is a prerequisite to engendering trust that China will be a long-term customer for oil and gas in this region. Furthermore, establishing these economic interests with its neighbors to the west necessitates protection of those assets if they become threatened. The multilateral military exercises conducted by the SCO,<sup>198</sup> as well as the PLA deployment exercises in China's western Xinjiang province,<sup>199</sup> imply that China could employ military force to protect its energy assets in Central Asia.

### ***An Emergency Oil Supply***

While building up its military power and expanding its soft power influence, China also is taking steps to respond to future supply disruptions by establishing national petroleum reserves. During the period of the 10<sup>th</sup> Five-Year Plan (2001–2005), the Chinese government decided to establish a strategic petroleum reserve (SPR) and identified four sites for storage: Zhenhai, Dalian, Zhoushan, and Huangdao. By 2008, the first phase will be completed and China will have reserves equal to 25 days of net oil imports.<sup>200</sup> By the completion of the second phase, China will have reserves equal to 42 days of net oil imports, or 200 million barrels.<sup>201</sup> When completed, these two facilities combined will have a capacity of 390 million barrels.<sup>202</sup> In March 2007 China announced that it may build a fifth storage tank in Lanzhou to hold crude oil imported from Kazakhstan.<sup>203</sup> China already has stored more than 37 million barrels in the Zhenhai tanks.<sup>204</sup> The Zhoushan storage terminal on the Aoshan Islands in Zhejiang province began accepting deliveries of crude in May 2007.<sup>205</sup>

Dr. Erica Downs of the Brookings Institution noted in a monograph on China's energy security that as of the end of 2006, China has not delineated its policies for using its strategic reserves.<sup>206</sup> Management of the SPR falls under the State Oil Stockpiling Office and State Oil Stockpiling Center that are subordinate to the National Reform and Development Commission, but the nature of this bureaucracy and its relation to the operation of the SPR is unclear.<sup>207</sup> Furthermore, it has been reported that the government increasingly is involving some of its major oil companies in the SPR activities and operations. For example, CNPC and Sinopec have been put in charge of constructing the SPR sites,<sup>208</sup> and *The Economist* reports that Sinopec has been given control over a third of the storage capacity at the Zhenhai storage facility.<sup>209</sup>

The lack of transparency in SPR operational policies and the involvement of China's oil companies in their operation have fueled concerns that Beijing may use its stockpiled oil to manipulate international prices. This has caused concern that one of China's considerations in deciding when to release reserves may be maximizing profits for its state-owned energy companies.<sup>210</sup> It also is possible, however, that the oil companies' involvement is nothing more than the government looking to its national energy companies to provide technical expertise its own bureaucratic organizations may lack.

In the 2006 U.S.-China Energy Policy Dialogue, U.S. officials emphasized the importance to the global petroleum market of using strategic reserves only during severe market disruptions and not to control domestic market prices.<sup>211</sup> Assistant Secretary of Energy for Policy and International Affairs Karen Harbert testified that at a meeting of energy ministers in December 2006, China expressed its intention to use its strategic reserves to ease adjustment to supply disruptions and not as a “market management tool.” Regardless, the U.S. Department of Energy is urging China to make a public commitment to coordinate drawdown of its strategic reserves with other nations and in coordination with the International Energy Agency.<sup>212</sup>

### **Implications for the United States**

The implications for the United States of China’s strategy for energy security are multifaceted. First, China relies on the United States to secure the sea lanes through which its energy supplies are shipped, and does not contribute to this effort. Essentially, China is able to be a free rider—receiving the benefit of U.S. protection of the sea lanes through which its energy supplies transit—while it simultaneously funnels available naval funds into a modernization program to develop a blue-water fleet.

Additionally, China’s allegiance to an oil equity ownership policy runs contrary to the approach of industrialized nations that rely on the free market to ensure an efficient distribution of oil supplies, and it reduces the ability of the market to respond quickly to political and natural disruptions in the global oil supply.

The relationships China forms and maintains with oil-producing countries such as Iran and Sudan in order to obtain oil supplies from them do not serve the interests of global peace and security or human rights. Mr. Helvey testified that “[a]n immediate consequence of this behavior is the negative impact that this has on U.S. goals favoring the spread of democracy, as well as priorities for the promotion of human rights and the rule of law, confronting the threat of terrorism, and non-proliferation.”<sup>213</sup> Oil revenue received from China props up these regimes and thwarts multilateral efforts to get the leaders of these nations to comply with international standards of behavior.<sup>214</sup>

### ***Improvements in the U.S.-China Strategic Energy Relationship***

Witnesses testified that China is starting to conclude that its approach to energy security will not provide the level of security Beijing desires.<sup>215</sup> China knows, of course, that it cannot meet its energy needs through domestic supplies of coal, natural gas, and oil, and thus must import energy sources. China’s equity petroleum assets abroad currently are sufficient to supply only a very small portion of its overall demand for imports, and China will not be able to meet its needs through this strategy alone.<sup>216</sup>

Mr. Herberg noted that China is beginning to see the pragmatic appeal of a multilateral approach to energy security, and to change its strategy for pursuing energy security. He also told the Commission that China’s demand is rising too quickly to be addressed effectively through equity investments, and that policy advisors in

Beijing are starting to suggest that the government instead focus on the stability of the market. Additionally, he testified that:

*[T]here is a growing sense in Beijing that the investment interests of China's [national oil companies, or] NOCs in expanding abroad are not necessarily synonymous with China's national energy security interests. ... There is growing discussion that, while China should have strong, globally competitive national oil companies commensurate with other global powers, China's energy security interests do not require heavy state support or unnecessarily controversial financial and diplomatic support for [its] NOCs.*<sup>217</sup>

Moreover, he noted that China is beginning to focus on the patterns of its domestic energy consumption and promote energy conservation, energy efficiency, and demand-side reforms that open the door to international cooperation.<sup>218</sup>

This change could affect the U.S.-China strategic energy relationship because it allows the relationship to be predicated upon mutual interests such as sea lane security, global oil market stability, and climate change. To this end, Assistant Secretary Harbert testified, "As two major energy consumers and economies in the world, the United States and China have been cooperating to address energy security and climate change issues. ... Over the course of recent years, the two countries have come to recognize how interdependent our economic prosperities and energy security have become."<sup>219</sup> Deputy Assistant Secretary of Energy for International Energy Cooperation David Pumphrey further noted, "This is a process that we take one step at a time, and based upon the progress we have achieved thus far, I believe there are even greater benefits down this road for both nations in terms of energy security and a clean energy future."<sup>220</sup>

## Conclusions

- China's pursuit of equity oil acquisitions is contrary to international commercial practices related to energy that support use of the market, and allocation of available petroleum supplies through international cooperation in the event of an emergency.
- In pursuing some of its global energy interests, China aids regimes operating contrary to U.S. foreign policy interests, such as the genocidal government in Sudan and Iran's government that is attempting to develop its own nuclear capability.
- The bilateral relationships China is building around the world—many if not most of them largely motivated by its quest for energy supplies and other resources—have resulted in an increase of its global economic, political, diplomatic, and cultural influence that has the potential to challenge U.S. interests.
- China's naval modernization is targeted not only on a Taiwan scenario but also on protecting China's economic resource supply chains. As Chinese overseas investment grows, the government will have a greater stake in protecting these investments and the ability to transport to China the resources the investments are producing and its economy requires. This is a major determinant of China's naval modernization.